Supreme Court U.S.
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No. 01-909

In the

Supreme Court of the United States

BALTIA AIR LINES, INC.,
(shareholders, employees and creditors),

Petitioner,

v.

CANADIAN IMPERIAL BANK OF COMMERCE and
CIBC OPPENHEIMER CORP.,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO
THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

REPLY TO RESPONDENTS BRIEF IN OPPOSITION

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REPLY TO OPPOSITION

CIBC's reply highlights their fear that Baltia's complaint will ever be granted access to an evidentiary hearing. Only by defeating access to the federal courts through protective contractual clauses designed to prevent disclosure, can CIBC retain its claimed absolute right, as the middleman clearing agent, to control the flow of capital investment.[1]

CIBC relies on the inability of the SEC to effectively intervene, and the courts' natural reluctance to enter a void. The void is § 17 A(b)(6).[2] Does it mean what it says? Or can it be ignored with impunity on the basis of technical legal rules which might, if applied in a blanket, inapposite manner, prevent the remediation of a vicious wrong Congress intended to prevent.

I. Certiorari Needed to Properly Define and Resolve the Meaning and Impact of Section 17 (A)(b)(6)

A. The Language of the Section, Identifying a Protected Group and Defining Prohibited Conduct, Demonstrates Congressional Intent to Create a Private Cause of Action

Unlike the earlier provisions of § 17 A, which discuss rules of proceedings, participants, schedules, applications and registrations, (b)(6) directly and simply identifies a group of persons that it protects, those who seek access to clearing services offered by any participant therein. This identification of a specific group of individuals to be protected is indicative of the intent of Congress to create a private cause of action. *California v. Sierra Club*, 451 U.S.

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[1] "CIBC Oppenheimer in its absolute discretion can refuse to accept any client, can refuse to clear any particular transaction." Transcript, U.S. District Court, p.3, l.13-15; (Reply App.)

[2] All Sections cited in this Reply Brief refer to the Securities Exchange Act of 1934, as amended, 48 stat. 881, 15 U.S. Code, Secs. 78a-78jj. (Commonly, "Exchange Act")

287 (1981). By identifying a duty to these specific individuals and prohibiting its violation, this provision fits the design of private litigation as an effective means of sanctioning and deterring the prohibited conduct. In addition, this is the only way a wronged party can be compensated for a violation.

In §27, Congress directed that suits to enforce duties, which would include the duty to provide access to services, be brought in the district court and, in §21D(e), Congress displays an intent that monetary damages, if proven, be awarded. In its Reply, CIBC suggests that these remedies are only available to investors to complain of violations of the Securities Act. (Reply, pages 15, 16) Yet, without an issue and an issuer, there is no need for clearing services at all.

Section 17A(b)(6) does not say "participant" or "issuer" or "investor" or "buyer" or "seller" which Congress could have easily specified. It says "person." While not controlling, the agency charged with overseeing the Act, the SEC has specifically recognized issuers as "persons" within the meaning therein.[3]

By defining the group protected and prohibiting specific conduct, the only rational meaning of this statute is to give both investors and issuers the right to litigate the discretionary limiting of access by a clearing agent, precisely as was done by CIBC to Baltia in this case. As currently interpreted by the courts below, §17A(b)(6) as a "mandate would lose all meaning if a party who continuously objected to an uncorrected categorical violation of the mandate could obtain no relief at the end of the day." *Lexecon v. Milberg*, 523 US 26, 43 (1998).

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[3] Securities Exchange Act Release No. 11604 (Aug 19, 1075), footnote 7:
"Clearing agencies, under Section 17A(b) (6), may not prohibit or limit access by any person to services offered by any participant therein. Persons having or seeking access to facilities of a . . . registered clearing agency include issuers of securities."

B. Section 17 A (b)(6) Creates a Relationship and A Duty Which Contracts Cannot Void

CIBC's alleged absolute contract right to deny access, at will, without the due process proceedings set forth in §17A(b)(5), is, on the one hand, a rules violation properly enforced and sanctioned by the SEC under *Brawer*, yet the practice of denying access is a statutory violation. Congress did not include §17A(b)(6) in the SRO rules. *See* §17A(b)(3). A contract made in violation of a statute is void. *Ewert v. Bluejacket*, 259 US 129, 138 (1922); *Waskey v.Hammer*, 223 US 85, 94 (1912); *Connolly v. Union Sewer Pipe Co.*, 184 US 540, 548 (1902).

CIBC in its Reply (pages 17, 22) argues that even if parts of its contract were illegal, Baltia would only be entitled to rescission or the "voiding" of the contract, rather than the provisions Baltia complains of, which allegedly allow them to escape the applicability of federal law, Paragraph VII(F), (Record A-65), and the provisions which allegedly allow them to discriminate at will, Paragraph I(D) and III(F.) (Record A-49, 53) (Reply, page 4). Congress expressly made any contract, or any practice, in violation of any provision of the Securities Exchange Act of 1934, void as to the person engaging in such practice. § 29(b). Even without the savings clause contained in CIBC's contract with Baltia's underwriter (Record A-65), § 29 ensures that only those illegal provisions of such a contract are void.

By statute, in § 17A(b)(6), Baltia is the intended third-party beneficiary of the participation contract between CIBC and H&W.[4] By § 17a(b)(6), CIBC was made a classic fiduciary — a person having duty, created by his undertaking, to act primarily for another's benefit in matters

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[4] The CIBC - H&W contract is the legal vehicle by which H&W became a participant in CIBC's clearing agency, with inherent statutory rights and limitation. The CIBC - H&W contract is not a commercial contract for unregulated services provided by CIBC. For accuracy, Baltia refers to the CIBC-H&W contract as a "participation agreement."

connected with such undertaking. *Basic Inc. v. Levinson*, 4865 US 239 (1988), n. 17, and related cases agree that where a fiduciary relationship exists, there is a duty to disclose. CIBC cannot contract to void the relationship or the duty.

Furthermore, the language cited from CIBC's boiler-plate contracts as the source of its absolute right does not apply to Baltia. Baltia never was, nor asked to be, an account of CIBC. There is no allegation that any securities transactions at issue were syndicated in any manner. The whole section cited by CIBC about advance written notification relates only if brokers "enter into, or join, a syndicate."

C. *Brawer v. Options Clearing Corp.* Does Not Decide Whether 17A(b)(6) Gives Rise to A Private Cause of Action.

In its Reply, CIBC relies on *Brawer v. Options Clearing Corp.*, 633 F. Supp. 1254, *aff'd*, 807 F. 2d 297, *cert denied*, 484 US 819 (1987) for the proposition that §17 A(b)(6) is intended to be enforced by the SEC. In fact, the *Brawer* court did not interpret that provision, but considered a private suit against self-regulatory organizations (SRO), for breaking their own rules when they did not adjust option prices on a security. The *Brawer* court interpreted §17 A(b)(3) and ruled that Congress displayed an intent that the SEC enforce the rules enacted by self-regulatory organization (SRO).[4]

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[4] Each clearing agency's rules are submits with an application registration and become terms of the clearing agency's license. In §19(h)(1), the SEC is authorized to suspend or revoke the license of a clearing agency or suspend any of the privileges conferred by that license.

II. Certiorari Should be Granted Because There is No Other Effective Remedy for Fundamental Wrongdoing

In its Reply, CIBC argues "standing" as its principal line of defense because it fears that its actual conduct would not bear any effective legal scrutiny. By seeking to contractually obscure access to federal review, with its undisclosed contracts and third party beneficiary limitations, it seeks to hide conduct which would be easily condemned if revealed. Baltia seeks merely the right to expose the alleged illegal conduct to a federal court which will then evaluate it and judge it in accordance with federal law.

The SEC cannot effectively monitor and prevent illegal conduct as alleged in Baltia's complaint, because the investigation proceeds so slowly and no remedy can be fashioned until after the fact of a violation. Since no financial remedy is available to an injured party, the wrong will be uncompensated, and therefore, largely undeterred. In addition, the illegal use of its controlling power by a clearing agency can be expected to be quite judicious, striking only in such cases as in Baltia's, where the theft and payoff is able to be effectively hidden, and the time frame so critical that the offense can be easily forgotten in the ebb and flow of the capital markets.

The broker dealers cannot effectively complain as their interests are inextricably divided between numerous investors and their client issuers, some of whom may be "favored" by the clearing agent and others which the clearing agent may choose, illegally, to diminish. They cannot afford to complain too much about a single transaction or offering.[6]

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[6] CIBC graciously cleared other of Baltia's underwriter's transactions after refusing Baltia's, placing the underwriter in the difficult situation, complaining and accepting, while also seeking to change its clearing agency. After it was able to change agents, it commenced an action against CIBC. Currently, the underwriter's arbitration against CIBC lingers on.

Section 17A(b)(6) makes Baltia the intended third-party beneficiary of the participation contract between CIBC and H&W. Section 17A(b)(6) makes CIBC the classic fiduciary — a person having duty, created by his undertaking, to act primarily for another's benefit in matters connected with such undertaking. *Basic Inc. v. Levinson*, 4865 US 239 n. 17(1988) and related cases agree that where a fiduciary relationship exists, there is a duty to disclose. As a fiduciary, CIBC owes Baltia, and like protected persons, a duty to disclose any material fact that would prevent clearance of an otherwise legitimate securities transaction. With recognition of the legal relationship established by § 17A(b)(6), § 18a becomes a viable cause of action.

CIBC claims that if Baltia's interpretation is upheld, it will be forced to engage in a careful screening of brokers, in order to exercise its discretion to screen out fraudulent trades. (Reply, pages 20, 21) This specious argument ignores the fact that the clearing agency acts in a different role from the broker/dealers, upon whom Congress imposed distinct obligations. § 3 (a)(4,5) and § 15. Guaranteed access does not force knowing participation in fraud or clearance where funds are insufficient or error exists,[7] but eliminates abusive, self-serving conduct which the statute was enacted to prevent.

CONCLUSION:

There is no doubt Congress intended 17A(b)(6) to mean something. CIBC will win if Baltia, its shareholders and employees are not "persons" within the meaning of that provision, and the US securities system, as enacted, recognizes no legal relationship between a clearing agent and the beneficiary of its contract to provide clearing services.

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[7] CIBC mentions "financial unfeasible" trades. The limited functions of a clearing agency make it incapable of determining the feasibility of a securities transaction. Congress tasked broker/dealers with effecting securities transactions. §3(a)(4) and (5).

Litigants such as Baltia will rarely be able to seek redress because in the US securities system, power is so intensely concentrated and unequal. The SEC has neither time nor resources to address this issue. Broker underwriters will be unable to effectively complain because they are so dependent on clearing agents.

This court has a special responsibility to ensure access to judicial review, especially when no effective remedy would otherwise exist to correct a potential grievous wrong.

Unless fully briefed, this case will be cited for the proposition that contracts between a clearing agency and a broker do not have to comply with § 17 A(b)(6), and that contracts preventing exposure of violations can effectively serve as a shield against wrongdoing. Clearing agencies will slowly and perniciously assert their ability to control distribution of capital, at will. Wronged parties will recognize the futility of complaint, and our system will continue its dangerous devolution towards the unmonitored concentration of power.

Unabated, the termite gnawing at the timber of the federal securities system will continue its gentle feast. Baltia asks that, as Congress intended, it be permitted, as the wronged party and the only party able properly do so, to investigate, litigate and perhaps expose this activity.

Respectfully submitted,

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REPLY APPENDIX

RELEVANT PORTIONS OF TRANSCRIPT DATED JUNE 14, 2000

United States District Court
Southern District of New York

00 Civ. No.: 678 (AKH)

Baltia Air Lines, Inc.
Plaintiff
v.
CIBC Oppenheimer Corp. et al
Defendants
Before:
Hon. Alvin Hellerstein, District Judge

Appearances

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The Court: . . . I used to represent Loeb Rhodes a number of years ago. It is nice to see they have revived themselves.

As I remember Rule 405 of the Stock exchange rules required that clearing agents become brokers of the customers directly. Is that still operative? It is part of the know-your-customer rule.

Mr. Schaffer: If they have agreed to clear for the customer of an introducing account, I believe that is correct.

In this case, of course, CIBC Oppenheimer never agreed to accept Baltia Airlines as a client in any way and never agreed to clear any transaction.

The Court: Implicit in the whole relationship of clearing agent and introducing broker is the right of the clearing agent to decide who is its customers.

Mr. Schaffer: That is exactly right.

The Court: Otherwise, you couldn't very much have liability, regulatory liability, of a clearing broker if the clearing broker was forced to take the customers of the introducing broker.

Mr. Schaffer: Precisely. That is why the agreement here provides that CIBC Oppenheimer in its absolute discretion can refuse to accept any client, can refuse to clear any particular transaction.